IN THE

Supreme Court of the United States

OCTOBER TERM, 1941

No. 524

HARRY STEIN, t/a JEAN CHEMICAL CO.

and

NATIONAL UNION INDEMNITY COMPANY,

Petitioner,

vs.

UNITED STATES OF AMERICA

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF

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To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petition of Harry Stein, trading as Jean Chemical Company and National Union Indemnity Company, a corporation, respectfully represent:

That on January 8, 1940, the District Court of the United States for the Eastern District of Pennsylvania entered judgment against the petitioner, National Union Indemnity Company, particularly on a bond executed by the petitioner in support of a permit issued to Harry Stein, trading as Jean Chemical Company, for the purpose of protecting the government of the United States against loss of taxes due on alcohol denatured under the provisions of the

Act of 1906, and permitted to be withdrawn tax free pursuant to such provision if in the event such tax free alcohol so withdrawn should be diverted to beverage purposes.

The facts are that the principal Stein applied for and received a permit to withdraw alcohol tax free under the provisions of the Act of 1906 (c. 3047, 34 Stat. 217), pursuant to which application a permit was duly issued to Stein and he withdrew under the terms thereof certain quantities of specially denatured alcohol for the purpose of using the same in the manufacture of toilet preparations, the formulae of which had been duly approved by the Division of Technology, Bureau of Internal Revenue, Treasury Department, Washington, D. C.

Thereafter on various dates in June of 1928, Stein withdrew certain quantities of specially denatured alcohol for the purpose of manufacturing the same in various designated toilet preparations, using the entire quantity of specially denatured alcohol so withdrawn in such manufacture. At the time of the manufacture involved, agents of the Prohibition Unit, then so designated, were present to witness such manufacture for the purpose of observing as to whether or not the quantities of alcohol withdrawn by Stein were actually consumed in the manufacture of the commercial toiletry products approved for manufacture by the Bureau of Internal Revenue.

The government contended that the manufacturer, Stein, while consuming and using the quantity of alcohol so withdrawn in the permitted manufacture, deviated from the approved formulae by injecting or introducing into the product an essential oil of an inferior quality, and that thereafter, upon completion of manufacture, sold his product to persons whose purpose it was to sell the same to other persons who had in mind the objective of manipulating the manufactured product in such a way that by the process of simple distillation, foreign ingredients such as essential oils and the basic ingredients of the specially de-

natured alcohol formula, might be readily removed to the end that a potable distillate fit for beverage purposes might be obtained and the resultant effect produce a taxable potable beverage diverted from industrial or commercial purposes to beverage purposes.

The Statement of Claim filed by the government, Record Page 16 claims for its first cause of action that the principal, Stein, pursuant to permit duly issued, executed a bond with the present petitioner, National Union Indemnity Company, as surety, on or about April 18, 1928, which bond was made part of the Record in the District Court and which appears, insofar as the obligatory part thereof is concerned, in the Record on Page 17. The Statement of Claim contended that between the 4th day of June and the 4th day of August, 1928, the principal of said obligation, diverted to beverage purposes 4472 wine gallons of specially denatured alcohol withdrawn tax free, but to which a tax would attach in the event that said alcohol so withdrawn was used for beverage consumption, the Statement alleging further that the principal failed to pay the tax of $2.00 per wine gallon attaching to such alcohol unlawfully diverted, lost or unaccounted for in violation of the terms of his permit and of the obligation of the bond. As for a second cause of action in the said Statement of Claim, the government alleged that between the dates of June 4th, 1928 and August 4th, 1928, the said Harry Stein, principal on the said bond, withdrew 4472 wine gallons of specially denatured alcohol free of tax in accordance with Section 11, Title III, Act of October 28, 1919 (41st Stat. 321), alleging that basic taxes as provided by various provisions of the Internal Revenue Laws would apply to the extent of $1.10 per proof gallon of such specially denatured alcohol withdrawn tax free and diverted to a use either unaccounted for or unauthorized. In Paragraph 19 of the Statement of Claim, the claimant contends that by reason of the said diversion and failure to account for the said 4472 wine gallons specially denatured alcohol withdrawn

by the principal on said bond, said principal wilfully attempted to defeat and evade and did defeat and evade payment of the taxes levied by Statute and more particularly referred to in other portions of the Statement of Claim, Record Pages 16 to 22.

The petitioner contends that the evidence below and particularly that evidence set out in the Appendix of the Appellant's Brief in the record filed with the Circuit Court Pages 31 to 39 does not in any way sustain the finding that the principal Stein in any way diverted actually or indirectly by cooperation with persons whom he knew intended to divert, and therefore the penal obligation of the bond is not involved, since the evidence could not tend to sustain measurable damages based on the tax rate applicable to alcohol used for beverage purposes.

There are certain Sections of the Internal Revenue Laws including Titles 2 and 3 of the National Prohibition Act, which are hereinafter set forth, Act, c. 85, 41 Stat. 305, Sections 4, 5, 9 and 29.

STATEMENT OF QUESTIONS INVOLVED

1. The Court erred in its finding of fact that the evidence tended to sustain tax liability on the part of the principal and hence the National Union Indemnity Company, as surety.

2. The Court erred in its conclusions that the cause was not a tax suit but was instead a suit on a bond.

3. The bond did not become operative until such time as tax liability was established on the part of the principal.

4. The government not having established tax liability upon the part of the principal within the period of limitation could not thereafter proceed against either principal or surety for the collection of taxes, the amount of which had not been liquidated or determined within the period of the Statute.